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UNCLAS SECTION 01 OF 02 MUSCAT 001582

SIPDIS

SENSITIVE

STATE FOR NEA/ARPI, EB/ESC/IEC, INR/EC

E.O. 12958: N/A
TAGS: ECON EFIN ENRG EPET PGOV SOCI MU
SUBJECT: WINDFALL FOR SOME, INFLATION FOR ALL

REF: A. STATE 186514
¶B. MUSCAT 1473

¶1. (U) Summary: Increasing oil prices have provided a windfall for the Omani government, even as its production declines. Consumer prices have risen accordingly, however, and some question whether the benefit of higher oil revenues is reaching the general public. End summary.

REVENUE UP, PRODUCTION DOWN

¶2. (U) According to the Ministry of National Economy's most recent figures, revenue from oil is up almost 50% over the first eight months of 2005, as compared to the same time period in 2004. Oil revenues contributed over $7.1 billion to state coffers from January to August 2005, as compared to $4.8 billion over the same period last year. The dramatic increase in revenues directly reflects the rapid increase in oil prices, as oil production actually fell 1.4% during the first eight months of 2005.

GOOD TIMES FOR ALL?

¶3. (SBU) Dr. Hatim al-Shanfari (protect), Professor of Economics at Sultan Qaboos University and board member of the Omani Economic Association, told Emboffs that increased oil revenues, while beneficial to the government's finances, have not been perceived by the general public as beneficial to their daily lives. Al-Shanfari remarked that one reason for this perception is the government's focus on large, capital-intensive industrial projects in a limited number of areas, such as in Muscat and Sohar. He is concerned that while the promoters of these industrial projects envision the larger companies creating "downstream" opportunities, appropriate mechanisms won't be in place to facilitate the establishment and growth of small and medium-size enterprises. Al-Shanfari lamented that oil production had robbed Oman of its traditional entrepreneurial spirit, and thus the government should channel funding toward educational awareness and training to restore it.

SQUEAKY WHEEL GETS THE SCHOOL

¶4. (SBU) Al-Shanfari also opined that oil revenue gains would enable the government to stall on meaningful internal reform. He noted that the Omani government previously has been able to use oil revenue to co-opt dissident segments of the population through public works projects, and that a flush treasury would allow the government to continue to stifle a new generation of leaders. Al-Shanfari also believes that spending on frivolous projects, such as the recent $2 million spent to upgrade a stadium's lighting and speaker systems, would add to inflationary pressures, especially in the areas of building materials and related construction costs. Spending of this nature gives al-Shanfari pause in predicting how the government would be able to manage its resources during a period of sustained low oil prices or other revenue crisis.

CONSUMERS FEEL THE PINCH...

¶5. (SBU) Dr. Said al-Riyami, Economic Advisor for the Ministry of Commerce and Industry, noted that as rising fuel prices have affected Oman's business community, the businessmen generally have passed the increased costs along to the consumers, making Oman more expensive as a result. He specifically pointed out that increased transportation costs have resulted in relatively larger price increases in Oman's interior regions. These increases have caught the attention of the Minister of Commerce and Industry, and as a result the Ministry is studying the issue more closely.

¶6. (SBU) Al-Shanfari noted that the government's Consumer Price Index survey, while procedurally sound, is artificially

weighted with inflation-proof inputs that lead to howls of disbelief each time the government announces new inflation figures. The government has commissioned a firm to re-examine the market basket used in the survey. Al-Shanfari estimates that true inflation rates for average Omani families are easily above 5 percent. Inflation in some sectors, such as construction materials, is even greater. A mid-level government official recently lamented to Emboff that the "dream house" he has been building should be finished in December, but construction costs have soared so high that he will now have to rent it out just to make ends meet.

...BUT IS IT ACTUALLY FROM OIL?

¶7. (U) The Ministry is interested in investigating the relationship between oil and consumer price increases. Commerce Ministry Under Secretary Ahmed al-Dheeb acknowledged before the press that the increase in oil prices and decline of the dollar (to which the Omani currency is tied) contributed to general inflation, but also questioned whether the greed of local businesses may also be playing a role. Al-Dheeb commented that "The Ministry will take serious measures against those who contribute to the rise in prices with no legitimate reason."

NO SUCH THING AS A FREE FILL-UP

¶8. (U) Increasing fuel costs have translated into higher prices at the pump for Omani drivers. However, fuel prices have risen in the UAE at an even higher rate, causing fuel shortages along Oman's northern border as UAE drivers cross the frontier for cheaper gas. In Buraimi, Oman's largest border town, 24-hour gas stations curtailed their operations as their fuel inventories ran out. One Omanoil salesman noted that rather than increase inventory, fuel suppliers actually decreased supplies to his company's station, causing a temporary barring of UAE taxis and commercial vehicles from fueling in Buraimi. While the situation has stabilized, Omani drivers are concerned that fuel hikes are fast approaching in their rear-view mirrors. The government already raised diesel prices by 43% in early May, which provoked a storm of complaints and parliamentary debate.

POLITICAL IMPLICATIONS

¶9. (SBU) The government has not raised public-sector salaries since the Omani riyal was tied to the U.S. dollar in 1986, using the purported lack of inflation as its justification. As noted ref B, popular expectations for a long-awaited salary increase have risen steadily in recent years, often cresting on national occasions such as the Sultan's annual address to parliament or the November 18 national day. With the bicameral parliament forming special committees to investigate price rises, the Ministry of Commerce's warning of price gouging, and the local media carrying feature articles on higher prices for essential Ramadan holiday cooking ingredients, the government has no cover on the inflation front. In view of hefty government surpluses, it also cannot plead poverty. Popular pressures for a gesture such as a pay increase are likely to build as both a way to offset the impact of rising costs and to share more broadly the current oil revenue windfalls. A more meaningful use of the windfall might be substantial increases in health care, education, and infrastructure investment in all regions of the country. Thus far, however, there has been little sign of government bending to these forces.
BALTIMORE